COMPANY RESEARCH AND ANALYSIS REPORT

TOKAI Holdings Corporation

3167

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Index

Summary

Led by the energy and CATV businesses, the Company is looking to post record-high profit for a third consecutive period in FY3/21

Based in Shizuoka Prefecture, TOKAI Holdings Corporation <3167> (hereafter, also "the Company") is a comprehensive lifestyle infrastructure company that is developing "energy and lifestyle-related services," primarily the provision of liquefied petroleum (LP) gas, and "information and communications services." In addition to realizing the Total Life Concierge (TLC; comprehensive services for living) concept*1, it began measures under the new ABCIR+S*2 theme in FY3/19, and is aiming to take a further leap forward while advancing an M&A strategy.

*1 Total Life Concierge concept: a vision that aims to improve customer satisfaction by providing comprehensive and detailed support for customers' comfortable lifestyles through the various services provided by the TOKAI Group.
*2 ABCIR+S: the TOKAI Group's strategy for technological innovation. It is the acronym of AI (A), Big Data (B), Cloud (C), IoT (I), Robotics (R), and Smartphone (S), and the Group will focus on creating and developing new services related to these.

1. FY3/21 3Q results

The Company reported FY3/21 3Q (April–December 2020) consolidated results of ¥139,792mn in net sales (down 1.2% year on year (YoY)) and ¥9,901mn in operating profit (up 6.7%). Net sales declined slightly due to lower sales prices in the energy business (LP gas and city gas business) and impacts on certain businesses caused by the spread of novel coronavirus infections (hereinafter, "COVID-19 pandemic"), but profit hit a record high for the second consecutive period due to factors including the rise in monthly billing revenue accompanying an increase in continuous-transaction customers, the effect of cost reductions related to procurement in the energy business, and a rise in profits from the corporate information and communications business. In addition, operating profit appears to have been approximately several hundred million yen above the Company's target. Furthermore, the Company boosted continuous-transaction customers by 130,000 YoY to 3,063,000 contracts at the end of December 2020.

2. Outlook for FY3/21

Regarding FY3/21 consolidated results, the Company maintained its initial targets of ¥205,300mn in net sales (up 4.8% YoY) and ¥15,000mn in operating profit (up 5.5%). The Company is aiming to increase the number of continuous-transaction customers by 102,000 to 3,105,000 contracts. Although net sales will likely fall short of the target due to the slight delay in acquiring commercial areas for LP gas and the impacts of the COVID-19 pandemic, we at FISCO feel there is room for a modest uptick on a profit basis. In the CATV business, Group companies are making optical conversion investments. The number of contracts for communications services is steadily increasing, and this is expected to drive the Company's earnings. The cross-selling rate (ratio of customers with multiple business transactions with the Company) was 19.7% at the end of FY3/21 3Q (versus 18.8% at the end of FY3/20), and is within range of the target of 20%. The Company plans to achieve growth from FY3/22 by continuing to expand continuous-transaction customer volume, seeking further M&A opportunities, implementing the ABCIR+S strategy, and deepening the TLC concept, among other efforts.

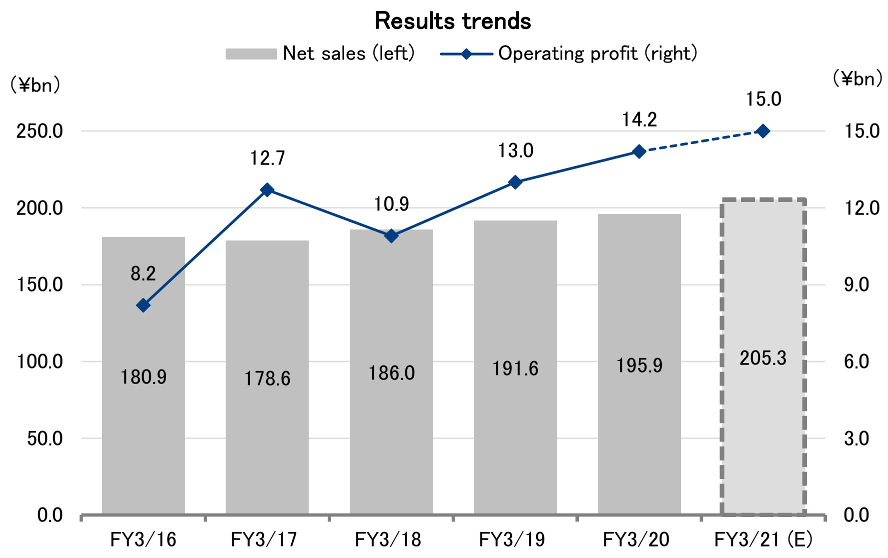
3. Update on progress in priority measures

Regarding the ABCIR+S strategy being promoted as a priority measure, the Company started an initiative in the Aqua business to prevent cancellations as a digital marketing measure using D-sapiens, a private DMP*, and launched an effort to promote increased sales of LIBMO (super-low-priced smartphones) to TLC members. Furthermore, in the spring of 2021, the Company will create a website for its LP gas service to promote digital membership of its customers, and will sequentially install automated metering using wireless communications technology. These initiatives are expected to boost operating efficiency, enable the optimization of service proposals to customers, and increase the cross-selling rate. In M&A strategy, the Company continues to take a proactive approach, and as a new business effort aimed at fleshing out the TLC concept, it is considering launching a healthcare service business via an alliance, and developments in this area should be monitored.

* DMP (Data Management Platform): a platform that handles centralized management and analysis of big data stored in various servers on the internet and log data from the Company's website, and ultimately optimizes an action plan for distributing advertisements and other measures.

Key Points

- Profit in FY3/21 3Q (April–December) hit a record high for the second consecutive period, and exceeded the Company's initial forecasts
- Profit is expected to exceed the Company's forecast for FY3/21, driven by earnings in the energy and CATV businesses
- The cross-selling rate is steadily increasing, and the Company aims to install an automated metering system for LP gas at 100% of its customers over the next five years



Source: Prepared by FISCO from the Company's financial results

Result trends

Profit in FY3/21 3Q (April–December) hit a record high for the second consecutive period and exceeded the Company's initial forecasts

1. Review of FY3/21 3Q results

The Company reported FY3/21 3Q consolidated results of ¥139,792mn in net sales (down 1.2% YoY), ¥9,901mn in operating profit (up 6.7%), ¥9,929mn in recurring profit (up 4.8%), and ¥5,936mn in net income attributable to owners of the parent (up 16.3%).

FY3/21 3Q consolidated results

(¥mn)

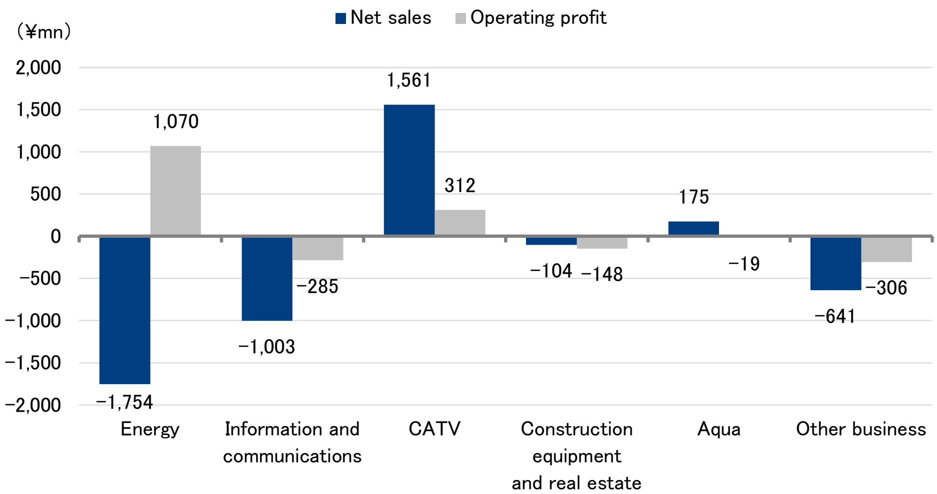
	FY3/20 3Q		FY3/21 3Q		
	Results	% of sales	Results	% of sales	YoY
Net sales	141,557	-	139,792	-	-1.2%
Cost of sales	84,254	59.5%	80,147	57.3%	-4.9%
SG&A expenses	48,024	33.9%	49,743	35.6%	3.6%
Operating profit	9,278	6.6%	9,901	7.1%	6.7%
Recurring profit	9,478	6.7%	9,929	7.1%	4.8%
Extraordinary loss	-1,465	-	-153	-	-
Net income attributable to owners of the parent	5,103	3.6%	5,936	4.2%	16.3%
Number of continuous-transaction customers (End-FY3/21 3Q, thousands)	2,933		3,063		4.4%

Source: Prepared by FISCO from the Company's financial results

Despite sales boosts from an increase in continuous-transaction customer volume (up 130,000 YoY to 3,063,000 contracts) and expansion of the corporate information and communications business, net sales eased compared to the same period of the previous fiscal year, on lower sales prices accompanying a decline in gas procurement prices (with no impact on operating profit) and delays in sales activities amid the COVID-19 outbreak. Although some businesses were affected by the impacts of the COVID-19 outbreak, each profit item hit a record high for the second consecutive period. This was due to an increase in monthly billing revenue related to higher customer volume, a rise in profits from the corporate information and communications business, and an improved profit margin in the LP gas business.

Looking at results by business segment, net sales increased in both the CATV and Aqua businesses, but declined in other businesses such as the energy business and information and communications business. Profit increased in the energy and CATV businesses, which made up for the decline in profit in other businesses. While net sales were approximately 4% lower than the Company's forecast, each profit line exceeded forecasts by more than 10%. In net sales, the energy, construction equipment and real estate, and other businesses caused net sales to fall short, while the energy, CATV, and Aqua businesses pushed profit higher.

Changes in business results by business segment (YoY)



Note: Segment names were changed from FY3/21 1Q
Note: Operating profit is prior to allocating indirect costs and other expenses
Source: Prepared by FISCO from the Company's financial results and results briefing materials

Profits driven by the energy, CATV, and the corporate information and communications businesses

2. Trends by business segment

Net sales by segment

(¥mn)

	FY3/18 3Q	FY3/19 3Q	FY3/20 3Q	FY3/21 3Q	YoY
Energy	53,145	54,675	55,191	53,437	-3.2%
Information and communications	37,760	37,959	38,834	37,831	-2.6%
CATV	20,871	22,829	23,433	24,994	6.7%
Construction equipment and real estate	13,491	13,846	14,919	14,815	-0.7%
Aqua	4,652	5,279	5,603	5,778	3.1%
Other business	3,415	3,352	3,575	2,934	-17.9%
Total	133,336	137,943	141,557	139,792	-1.2%

Source: Prepared by FISCO from the Company's financial results

Operating profit by segment

(¥mn)

	FY3/18 3Q	FY3/19 3Q	FY3/20 3Q	FY3/21 3Q	YoY
Energy	3,857	2,954	3,964	5,034	27.0%
Information and communications	2,410	2,595	3,366	3,081	-8.5%
CATV	2,758	3,568	3,790	4,102	8.2%
Construction equipment and real estate	681	915	1,242	1,094	-11.9%
Aqua	221	444	597	578	-3.2%
Other businesses and adjustments	-3,350	-3,442	-3,682	-3,988	-
Total	6,579	7,038	9,278	9,901	6.7%

Note: Values are prior to allocating indirect costs and other expenses
Source: Prepared by FISCO from the Company's financial results and results briefing materials

Number of customers by key service

(thousand)

	End of FY3/18 3Q	End of FY3/19 3Q	End of FY3/20 3Q	End of FY3/21 3Q	YoY change
Energy	653	674	703	737	34
LP gas	599	620	647	676	29
City gas	54	55	56	61	5
Information and communications	818	797	766	763	-3
ISP	797	758	720	711	-9
(Existing ISP and related services)	478	430	396	375	-21
(Hikari Collaboration)	319	328	324	335	11
LIBMO	21	39	45	52	7
CATV	1,002	1,055	1,088	1,188	100
Broadcast service	751	785	801	871	70
Communications service	251	270	287	317	30
Aqua	143	157	160	162	2
Mobile	229	220	214	209	-5
Security	17	17	16	16	0
Total	2,839	2,898	2,933	3,063	130
(TLC member volume)	669	783	875	958	83

Note: The number of customers has been rounded to the nearest thousand. Information and communications and CATV both offer communications services, so total figures avoid duplication
Source: Prepared by FISCO from the Company's financial results and results briefing materials

(1) Energy business

The energy business reported ¥53,437mn in net sales (down 3.2% YoY) and ¥5,034mn in operating profit (up 27.0%; prior to allocating indirect costs and other expenses and hence different than the calculation method in the financial results (applies to all businesses below)). Factors increasing profit included the increase in customer volume (¥780mn), decline in procurement prices (¥680mn), and increase in consumption volume per household due to stay-at-home demand (¥270mn). Meanwhile, factors decreasing profit included higher customer acquisition costs (¥340mn) and an increase in personnel costs and other expenses (¥300mn). In total, there was a ¥1,070mn increase in profit. On a quarterly basis, net sales for the three months ended December 31, 2020 increased 3.0% YoY, marking the first increase in five quarters, while operating profit increased 32.7%, the first increase in two quarters.

The LP gas business recorded ¥45,135mn in sales (down 1.1% YoY) and a double-digit rise in operating profit due to an improved profit margin accompanying lower procurement prices and an increase in customer volume. The Company lifted customer volume by 29,000 to 676,000 contracts at the end of FY3/21 3Q, a stronger gain than the net addition of 27,000 contracts* a year earlier. Key positives were active acquisitions of commercial areas and steady recruitment of customers at 11 new area sites. There was an increase of 24,000 contracts from the beginning of the fiscal year. Of these, 16,000 contracts were in existing areas, while 8,000 contracts were from new areas. However, the acquisition of commercial areas was delayed due to the impacts of the COVID-19 pandemic, which resulted in the number of contracts falling around 12,000 short of the initial forecast.

* The Company opened a total of 11 sales sites including Sendai, Iwaki and Toyokawa in 2015, Nishimikawa and Gifu in 2016, Tajimi and Okayama in 2017, Fukuoka in 2018, Tsu in 2019, and Kasugai and Yokkaichi in June 2020.

The city gas business posted ¥8,301mn in sales (down 13.3% YoY) with setbacks from a decline in the average sales price under the system to adjust raw material costs and non-recurrence of sales from air-conditioning work at elementary and middle schools recorded in the previous year (widening the decline margin), while operating profit also declined. Customer volume improved by 5,000 YoY to 61,000 contracts as a result of the start of business in Nikaho City (Akita Prefecture) from a business purchase in April 2020.

(2) Information and communications business

The information and communications business posted ¥37,831mn in net sales (down 2.6% YoY) and ¥3,081mn in operating profit (down 8.5%). Despite higher sales and profit in the corporate business due to robust sales of services with recurring revenue, there was a decline in both sales and profit in the consumer business due to the drop in customer volume and higher customer acquisition costs. On a quarterly basis, net sales for the three months ended December 31, 2020 declined 1.7% YoY and operating profit fell 4.7%, however operating profit only fell short of the Company's forecast by a few tens of millions of yen.

The consumer business recorded ¥19,801mn in sales (down 8.6%). It appears that operating profit declined by a bit more than ¥500mn, with the main factors for the decline being the decrease in customer volume (¥260mn) and increase in customer acquisition costs (¥310mn). Looking at customer volume for each service at the end of December 2020, although the number of contracts increased by 7,000 YoY to 52,000 contracts for LIBMO and 11,000 to 335,000 contracts for Hikari Collaboration, contracts declined by 21,000 to 375,000 contracts for existing ISP services, which was a factor in the decline in sales. However, it should be noted that total contract volume increased by 2,000 contracts compared to the end of the previous year, marking the first such increase since FY3/15. In recent years, customer volume continuously dropped due to tougher competition with major mobile phone carriers, but sales promotion campaigns for Hikari Collaboration at top consumer electronics retailers had a big impact on capturing telework demand. The number of new contracts is increasing and the number of cancellations appears to be declining, so when it comes to Hikari Collaboration, the YoY increase for three consecutive quarters is a good sign. If contract volume continues to increase going forward, especially for Hikari Collaboration which has a high sales price per customer, there is a strong possibility that sales in the consumer business will increase YoY in FY3/22 1Q, marking the first such increase in four years. We will be keeping a close watch on future developments.

Meanwhile, in the corporate business, sales increased 5.0% YoY to ¥18,030mn, while operating profit increased by ¥220mn due to the impact of higher sales. While sales in the consigned system development business declined due to impacts of the COVID-19 pandemic and a recoil decline following large contracts in the same period of the previous fiscal year, this decline was offset by strong sales of services with recurring revenue due to capturing cloud service and telework demand.

(3) CATV business

The CATV business posted ¥24,994mn in net sales (up 6.7% YoY) and ¥4,102mn in operating profit (up 8.2%). With these results, progress towards full-year forecasts was ahead of schedule. SENDAI CATV CO., LTD., which was made a subsidiary in March 2020, added about ¥700mn–¥800mn in net sales (no impact on operating profit due to goodwill amortization charges), and sales rose by approximately 3% excluding this factor. In profits, higher profit from increased customer volume more than offset the increase in personnel costs and other expenses. In FY3/21 3Q alone, net sales increased 8.5% YoY and operating profit significantly rose 17.4%, of which just under ¥100mn was due to a corporate business tax refund.

Customer volume increased by 100,000 YoY (including 57,000 contracts from SENDAI CATV) to 1,188,000 contracts. This included an increase of 70,000 to 871,000 contracts for broadcast services and 30,000 to 317,000 contracts for communications services. Regarding communications services, Group companies are making investments in optical conversion, including compatibility with 4K broadcasts, and the number of contracts for the CATV-FTTH service is increasing.

(4) Construction equipment and real estate business

The construction equipment and real estate business recorded ¥14,815mn in net sales (down 0.7% YoY) and ¥1,094mn in operating profit (down 11.9%). The impact of the COVID-19 pandemic led to delays in sales activities, resulting in a decline in sales of renovation and facility equipment sales, which caused profit to fall more than ¥200mn short of the Company's forecast.

Operating profit at Nissan Tri-Star Construction, Inc.,*1 which was made a subsidiary in September 2019, was ¥100mn. Also, Chuo Denki Koji Co., Ltd.,*2 which was made a subsidiary in August 2020, and Inoue Technica Co., Ltd.,*3 which was made a subsidiary in November 2020, provided a combined operating profit of ¥80mn. With these M&A, as a general construction firm, the TOKAI Group has established a framework capable of comprehensively delivering civil engineering and construction work; internal work including air conditioning, hygiene, and electrical; and building maintenance services, and aims to further expand its scale of business in the Tokai region.

*1 Nissan Tri-Star Construction, Inc. is engaged in public works, general construction and other business in Gifu Prefecture, and has annual sales of around ¥2bn.
*2 Chuo Denki Koji Co., Ltd. engages in the electrical construction business in Aichi Prefecture with just under 30 employees.
*3 Inoue Technica Co., Ltd. provides building maintenance services in the eastern part of Shizuoka Prefecture, and has annual sales of approximately ¥500mn.

(5) Aqua business

The Aqua business recorded ¥5,778mn in net sales (up 3.1% YoY) and ¥578mn in operating profit (down 3.2%). Customer volume only increased by 2,000 YoY to 162,000 contracts because the Company had no choice but to refrain from sales activities at shopping malls and other facilities, its main sales channel, due to the impacts of the COVID-19 pandemic, but the increase in consumption volume per subscriber household due to stay-at-home demand led to the increase in sales. In profits, in addition to the increase in profit due to the rise in customer volume, there was a decline in customer acquisition costs (¥140mn), but the increases in costs accompanying organizational restructuring and higher logistics expenses were factors that reduced profits. For the three months ended December 31, 2020, net sales increased 2.5% YoY, while operating profit declined 33.0%, resulting in a decline for a second consecutive quarter. However, it appears that operating profit was just over ¥100mn more than the Company's forecast in conjunction with the decline in customer acquisition costs.

(6) Other business

Other business reported ¥2,934mn in net sales (down 17.9% YoY). Breaking this down, in the nursing care business, sales rose to ¥995mn (up 9.9%) with FY3/20's acquisition of Tender Co., Ltd., which operates a serviced senior residence (19 rooms). The shipbuilding business, meanwhile, posted a 5.8% decline in sales to ¥991mn due to a decline in ship repair projects, and sales in the wedding ceremony business fell significantly by 68.8% to ¥322mn, due to postponements and people refraining from holding banquets and other events due to the COVID-19 pandemic. The segment's operating loss, including internal adjustments, was ¥3,988mn (compared to a loss of ¥3,682mn in the same period in the previous fiscal year).

Outlook

FY3/21 earnings will be driven by the energy and CATV businesses, with profits expected to exceed the Company's forecasts

1. Outlook for FY3/21 consolidated performance

For FY3/21 consolidated results, the Company retained its initial forecasts for net sales to increase 4.8% YoY to ¥205,300mn, operating profit to rise 5.5% to ¥15,000mn, recurring profit to grow 2.7% to ¥14,870mn, and net income attributable to owners of the parent to climb 2.7% to ¥8,460mn. Progress rates through FY3/21 3Q were 68.1% for net sales and 66.0% for operating profit. When comparing these progress rates to averages for the last three years (72.0% for net sales and 59.9% for operating profit), the Company is falling slightly short for sales but exceeding the average by more than 10% for operating profit. For all profit lines, results were slightly higher than forecasts, and we at FISCO think it is very likely that the Company will post record-high profits for a third consecutive period.

Outlook for FY3/21

(¥mn)

	FY3/20 3Q		FY3/21 3Q			3Q progress rate	Average progress rate for the last three years
	Results	% of sales	Forecast	% of sales	YoY		
Net sales	195,952	-	205,300	-	4.8%	68.1%	72.0%
Operating profit	14,224	7.3%	15,000	7.3%	5.5%	66.0%	59.9%
Recurring profit	14,479	7.4%	14,870	7.2%	2.7%	66.8%	60.1%
Net income attributable to owners of the parent	8,241	4.2%	8,460	4.1%	2.7%	70.2%	55.2%
Net income per share (¥)	62.93		64.60		2.7%		
Number of continuous-transaction customers (thousands)	3,003		3,105		3.4%		

Source: Prepared by FISCO from the Company's financial results

The Company intends to continue raising monthly billing revenue by expanding continuous-transaction customer volume (forecasting an increase of 102,000 YoY to 3,105,000 contracts) and will build an earnings base supporting medium- to long-term Group growth by further promoting M&A, implementing ABCIR+S, and deepening the TLC concept. By business segment, the Company is anticipating higher profits particularly in the energy, information and communications, and CATV businesses, which are the Group's core business areas. With respect to customer volume, it will be difficult for the Company to completely recover in 4Q from the delays experienced through FY3/21 3Q, and there is a possibility that customer volume will fall by several thousand contracts below the forecast, but the customer base is still steadily expanding.

The results forecasts for the main businesses are described below.

(1) Energy business

In the energy business, while customer volume continues to increase, net sales will likely decline as a result of a decrease in sales prices. However, the Company expects profit for the full year to increase by around ¥1.4bn in FY3/21 as the profit margin continues to improve due to lower procurement prices.

The Company expects customer volume in the LP gas business to increase by 51,000 versus the end of the previous fiscal year to 703,000 contracts, but as of the end of FY3/21 3Q, there had only been an increase of 24,000 contracts. It seems the Company could reach an increase of more than 40,000 contracts versus the end of the previous fiscal year by focusing on acquiring commercial areas and cultivating customers in new areas during 4Q. Of these, it expects to acquire a total of 3,000 customers from new sites that opened in Kasugai and Yokkaichi in June 2020, where full-fledged sales activities commenced in FY3/21 4Q.

Conversely, in the city gas business, the number of customers is set to remain unchanged compared to the end of the previous fiscal period at 61,000 contracts. However, as the figure at the end of the previous period included the addition of 5,000 contracts in Nikaho City (Akita Prefecture) as a result of starting business in April 2020, in actuality, the number of customers will increase 9% YoY. The Company expects a drop in sales as the average sales price continues to decline.

(2) Information and communications business

The Company's outlook for the information and communications business is a modest increase in net sales and a ¥250mn rise in operating profit, but a slight contraction in profit growth is expected. When broken down, profit is forecast to increase just over ¥400mn in the corporate business and decline in the consumer business.

The number of customers in the consumer business is expected to change direction and increase, up 2,000 compared to the end of the previous fiscal period to 975,000 contracts. Breaking this down, they will decrease 21,000 to 368,000 contracts for existing ISP and related services, increase 13,000 to 337,000 contracts for Hikari Collaboration, increase 15,000 to 63,000 contracts for LIBMO, and decrease 5,000 to 207,000 contracts for mobile. Progress through FY3/21 3Q shows a decline of 14,000 contracts for existing ISP services, an increase of 11,000 contracts for Hikari Collaboration, an increase of 4,000 contracts for LIBMO, and a decline of 3,000 contracts for mobile. While the pace of the increase in LIBMO contracts is behind the forecast, Hikari Collaboration has slightly exceeded the plan. The factors behind the sluggish results for LIBMO in FY3/21 1Q included store closures due to the COVID-19 pandemic and the intensification of competition in the super-low-price smartphone market. Going forward, the Company hopes to catch up by promoting sales through a bundled plan with Hikari Collaboration.

In the corporate business, meanwhile, despite concerns about a shortfall in consigned system development, the Company expects both sales and profit to continue to increase due to the growth of recurring revenue, including network connectivity services aided by the expansion of the cloud services market.

(3) CATV, construction equipment and real estate, and Aqua businesses

In the CATV business, the Company was forecasting net sales to increase 6% YoY and operating profit to grow 2%, but through FY3/21 3Q, the rate of progress for both sales and profit was faster than anticipated and results for the full year are expected to exceed the plan. The number of customers is forecast to increase by 37,000 YoY to 1,191,000 contracts, but as of the end of FY3/21 3Q, the number of customers had increased by 34,000 contracts, which is slightly exceeding the plan. In its initial forecast, the Company had been expecting the profit margin to decline a bit due to efforts to reinforce personnel and an increase in depreciation costs accompanying optical conversion investments, but thanks to factors like the corporate business tax refund in 3Q, there is a strong likelihood that the profit margin will remain at around the same level as in FY3/20. Capital investment is expected to increase to ¥6,700mn from ¥5,300mn at the end of the previous fiscal year.

While the Company's initial plan projected higher sales and profit in the construction equipment and real estate business, the COVID-19 pandemic caused a decline in both sales and profit through FY3/21 3Q. However, orders have been gradually recovering, and M&A activity will have an impact, so the Company is aiming to achieve increases in both sales and profit for the full fiscal year as it initially forecast.

In the Aqua business, the Company forecasts a 6% YoY increase in net sales and a decline in operating profit. The Company had been forecasting a customer volume gain of 11,000 YoY to 172,000 contracts, but through FY3/21 3Q, there had only been an increase of 1,000 contracts, and it now looks like net sales will only increase by about 3%. Meanwhile, although there has been an increase in logistics costs, the Company expects operating profit to decline to roughly the level initially forecast as a result of the drop in customer acquisition costs and other factors.

Aiming for a steady increase in the cross-selling rate, and targeting a 100% installation rate for an automated LP gas metering system over the next five years

2. Update on progress in priority measures

(1) ABCIR+S strategy

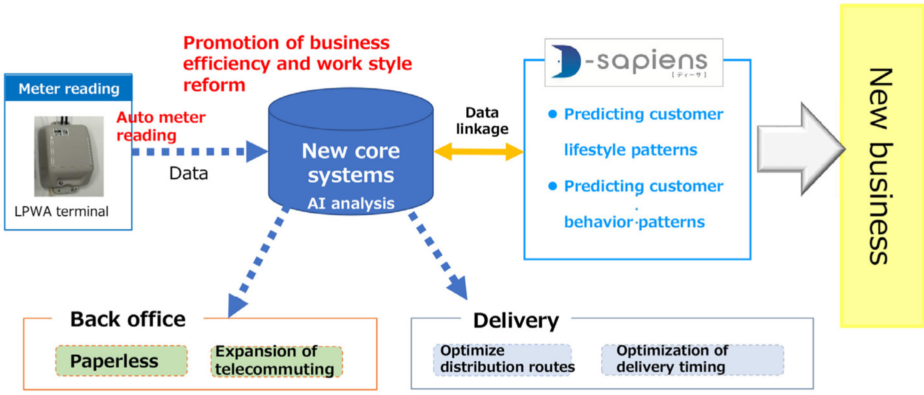
The Company has started conducting a full-fledged digital marketing effort utilizing the D-sapiens DMP, the foundation of its ABCIR+S strategy. In FY3/21 1Q, it implemented an initiative in the Aqua business to identify those likely to cancel their service based on AI analysis using customer behavior records stored in D-sapiens (web records, transaction records, inquiries, and other data) and dispense questionnaires with a benefit by direct mail to suspected customers. Through this effort, a 20% reduction in the churn rate was confirmed versus a group for which no action was taken.

In FY3/21 3Q, the Company launched cross-selling and retention campaigns that combine D-sapiens and the TLC Membership Service* targeting TLC members, including a campaign to expand LIBMO sales. Going forward, the Company plans to advance similar initiatives in all types of services, as it works to reduce the churn rate, increase the cross-selling rate, and maximize customer lifetime value. This is important because of a possible further increase in profitability if the cross-selling rate rises due to higher sales per customer and a decline in customer acquisition and maintenance costs. The cross-selling rate moderately increased from 18.8% at the end of March 2020 to 19.5% at the end of September 2020 and 19.7% at the end of December 2020, which is within the target range of the Company's near-term goal of 20%.

* The TLC Membership Service is a program that customers using the TOKAI Group's services can enroll in to earn reward points. Customers earn points based on their use of each service, and can use accrued points to pay their bills, convert points into e-money or transfer points to another point program. As of the end of FY3/21 3Q, there was a total of 958,000 members.

The Company also deployed and started operation of a new mission-critical system in the LP gas business in FY3/21, and is pursuing improved business efficiency and workstyle reforms. With a target of FY3/22 1Q, the Company will launch a dedicated website and work to convert customers into digital members. There is a decent number of LP gas customers who are not yet TLC members, and by enrolling these customers, the Company will promote digital marketing campaigns using D-sapiens. Furthermore, a notable development will be the initiative to construct an automated metering system utilizing LPWA devices. Installing these devices on customers' premises and automatically collecting usage volume data from gas tanks via wireless communications is expected to optimize delivery timing, improve delivery route efficiency, and boost efficiency of administrative division work, among other effects. Currently, the Company is introducing this system when new customers sign up and when existing, old equipment is replaced or updated. Its plan is for 6% of customers (just over 40,000) to be equipped with the system by the end of FY3/21, and to then raise the installation rate to 100% over the next five years or so. Investment in the new mission-critical system, including its construction, is planned to be a few billion yen, but improvements in delivery costs and other operations are expected to offset these investment costs and further expand market share.

Utilization of D-sapiens in the ABCIR+S strategy



Source: The Company's results briefing materials

(2) M&A strategy

As a result of the M&A strategy between the fiscal year ended March 2018 and September 2020, the Company has executed 13 deals, investing ¥12,989mn to secure ¥8,528mn in net sales, ¥618mn in operating profit, and 350,000 customer contracts. As mentioned before, Inoue Technica Co., Ltd., which operates a building maintenance business, was made a subsidiary in November 2020, and the Company is currently reviewing M&A opportunities for more than 20 deals totaling over ¥100bn in value. The M&A strategy has been impacted considerably by the COVID-19 pandemic, including limitations on opportunities for talks with counterparties, but the Company still plans to proactively pursue M&A.

M&A and alliance results (from 2017 through September 2020)

(¥mn)

Business	Number of companies	Investment value	Net sales	Operating profit	Number of customers
City gas	Four companies	1,953	626	42	6,000 contracts
CATV	Four companies	3,997	4,769	221	344,000 contracts
Information and communications	Two companies	655	398	67	-
Construction equipment and real estate	Two companies	3,394	2,735	288	-
Overseas*	One companies	2,992	-	-	-
Total	thirteen companies	12,989	8,528	618	350,000 contracts

* Overseas business refers to an alliance with a Vietnam-based LP gas sales firm that is handled as an equity-method affiliate.
Source: Prepared by FISCO from results briefing materials

(3) New business initiatives

The Company advocates the Total Life Concierge (TLC; comprehensive services for living) concept, which delivers safety and reliability, convenience and comfort, and happiness and purpose in people's lives, as a management vision and pursues creation of new businesses toward realizing this concept.

Specifically, the Company is considering healthcare services as a business. It envisions services to prevent cancer, lifestyle diseases, and other illnesses as well as promote health based on the importance of personal health in living a more prosperous and purposeful life. It wants to collaborate with companies that have customer bases in healthcare or with IT ventures, rather than conducting these services on its own, and jointly build a business model, including service content and other aspects. The Company obtained favorable reactions in a marketing survey conducted during August–September 2020. We will be closely monitoring developments in this area.

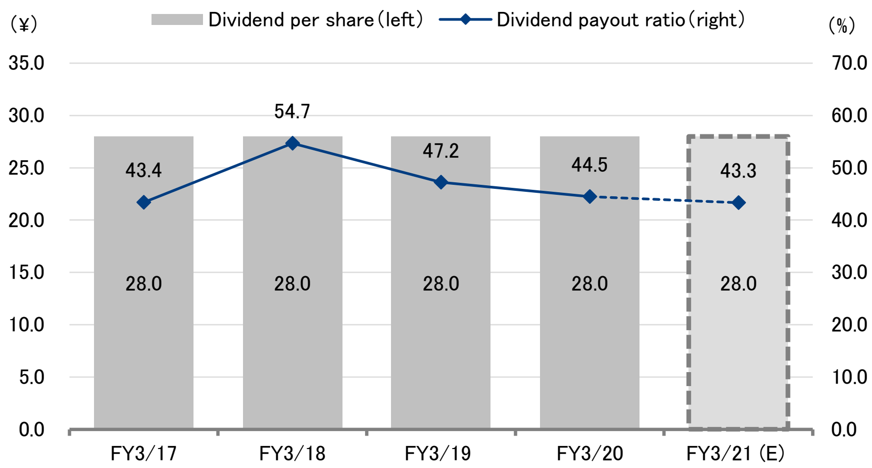
Shareholder return policy

Annual return on investment of 3% to 6% from dividends and gifts to shareholders

The Company returns profits to shareholders by paying dividends, presenting gifts, and purchasing treasury shares depending on conditions. Its basic policy is to continuously pay a stable dividend and it targets a dividend payout ratio of 40% to 50%. The FY3/21 dividend per share will remain unchanged YoY at ¥28.0 (for a dividend payout ratio of 43.3%).

The Company presents gifts to shareholders at the end of March and September depending on the number of shares held. For each unit of shares (100 shares) held, shareholders can receive one of the following gifts: an Aqua product worth ¥2,050 (such as Ulunom's natural water from Mt. Fuji, etc.), a QUO card worth ¥500, meal coupons worth ¥1,000, TLC Membership Service points worth ¥1,000, or a ¥2,100 discount on LIBMO usage fees (¥350 a month x 6 months). When including the gifts to shareholders in an estimate of the total investment yield per share unit from the current share price level (closing price of ¥1,000 on February 5, 2021), it is in the range of 3.8% to 6.9% (calculation based on selection from either a QUO card or an Aqua product as the gift).

Dividend per share and dividend payout ratio



Note: FY3/17 includes a ¥6.0 commemorative dividend
Source: Prepared by FISCO from the Company's financial results

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